

UNITED STATES OF AMERICA
DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT
OFFICE OF ADMINISTRATIVE LAW JUDGES

In the Matter of:

JEFFREY J. WIRTH AND
AFFILIATES,

Respondents.

HUDALJ 93-1942-DB(LDP)
Decided: November 12, 1993

Michael Kalven, Esquire
For the Department

Kenneth R. Hertz, Esquire
For the Respondents

Before: Thomas C. Heinz
Administrative Law Judge

INITIAL DETERMINATION AND ORDER

Statement of the Case

This proceeding arose pursuant to 24 C.F.R. § 24.700 *et seq.* as a result of action taken by Thomas T. Feeney, the Manager of the Minneapolis-St. Paul Office of the U.S. Department of Housing and Urban Development ("the Department" or "HUD") on September 30, 1992, imposing a twelve-month Limited Denial of Participation ("LDP") upon Mr. James Damiani, Mr. Eric Brynestad, Real Estate Exchange Company of Minneapolis (REECM), and Respondents Jeffrey Wirth and affiliates. The LDP prohibited the named parties from engaging directly or indirectly in the Department's property disposition programs within Minnesota. Mr. Feeney took action based on information indicating that Messrs. Damiani and Brynestad and REECM had participated in a scheme designed to permit Respondent Wirth to evade the terms of an earlier LDP issued against him and his affiliates on June 15, 1992.

Pursuant to requests, informal conferences with HUD were held for Respondent Wirth on October 21 and November 19, 1992, for Mr. Brynestad on November 3 and 23, 1992, and for Mr. Damiani on October 30 and November 25, 1992. After the conferences, the LDP against Mr. Damiani was terminated, and the sanction against the remaining parties was affirmed.

On December 14, 1992, Mr. Brynestad and Respondent Wirth and affiliates appealed the imposition of the LDP and requested a hearing (see 24 C.F.R. § 24.713). A hearing was held in Minneapolis, Minnesota, on April 6, 7, and 8, 1993, during which Mr. Brynestad, REECM and the Department reached a negotiated settlement.¹ At the close of the hearing, the parties were directed to file briefs. The last brief was received on August 6, 1993.

Findings of Fact

Jeffrey J. Wirth ("Respondent Wirth") is chief executive officer, president, and owner, with his wife, of approximately ten companies, including "The Wirth Companies" ("TWC"). (GX.1)² Respondent Wirth and his affiliated companies have offices at 7040 Lakeland Avenue North, #105, Brooklyn Park, Minnesota, and are engaged in the business of buying, selling, and managing real estate.

In April of 1993 Eric Brynestad ("Mr. Brynestad") had been an employee of Respondent Wirth for two and a half or three years and had held a real estate salesperson license for about two years. (TR. 173-176) Respondent Wirth has the power to fire Mr. Brynestad or change the conditions and terms of his employment at will. (TR. 155)

On June 15, 1992, the manager of the Minneapolis-St.Paul Office of HUD issued an LDP against Respondent Wirth and his affiliates prohibiting them from participating in HUD property disposition sales programs within Minnesota for one year. (GX. 15)

REECM is a Minnesota corporation that was formed by Respondent Wirth and his wife in 1991 for tax purposes. (TR. 157, 196) In July of 1992 the corporation was inactive and had no assets or liabilities; it was merely a shell. (TR. 166-68) According to stock transfer certificates in the record, Respondent Wirth and his wife assigned all of the issued and outstanding shares of the corporation to Mr. Brynestad on July 23, 1992. (RX. 14, 15) Respondent Wirth testified that the stock was transferred to Mr. Brynestad for the token sum of \$1.00, even though it would have cost Mr. Brynestad considerably more to form a new corporation on his own. (TR. 182)

¹The case style has been amended accordingly.

²The following reference abbreviations are used in this decision: "TR." for "Transcript;" "GX." for "Government's Exhibit;" and "RX." for "Respondents' Exhibit."

REECM submitted bids to purchase HUD-owned residential properties at 2712-14 Penn Avenue North and 2655 Knox Avenue North in Minneapolis on August 10, 1992, and August 26, 1992, respectively.³ Mr. Brynestad signed the bids as Vice-President of REECM and gave a telephone number and address for the corporation that are the same as the telephone number and address for Respondent Wirth and his affiliated companies. Mr. Damiani, also employed by Mr. Wirth as a real estate broker at the same location, was identified in the bids as the broker for the transactions. (GX. 23, 24)

Subsidiary Findings and Discussion

An LDP is a type of debarment. The purpose of all debarments imposed by agencies of the Federal government, including an LDP imposed by HUD, is to protect the public interest by precluding persons who are not "responsible" from conducting business with the federal government. 24 C.F.R. § 24.115(a). See also *Agan v. Pierce*, 576 F. Supp. 257, 261 (N.D. Ga. 1983); *Stanko Packing Co., Inc. v. Bergland*, 489 F. Supp. 947, 948-49 (D.D.C. 1980). The debarment process is not intended to punish; rather, it is designed to protect governmental interests not safeguarded by other laws. *Joseph Constr. Co. v. Veterans Admin.*, 595 F. Supp. 448, 452 (N.D. Ill. 1984). In other words, the purpose of debarment is remedial, not punitive. See 24 C.F.R. § 24.115.

In the context of debarment proceedings, "responsibility" is a term of art that encompasses integrity, honesty, and the general ability to conduct business lawfully. See 24 C.F.R. § 24.305; *Gonzalez v. Freeman*, 334 F.2d 570, 573 & n.4, 576-77 (D.C.Cir. 1964). Determining "responsibility" requires an assessment of the current risk that the government will be injured in the future by doing business with a respondent. See *Shane Meat Co., Inc. v. U.S. Dep't of Defense*, 800 F.2d 334, 338 (3d Cir. 1986). That assessment may be based on past acts. See *Agan*, 576 F. Supp. 257; *Delta Rocky Mountain Petroleum, Inc. v. U.S. Dep't of Defense*, 726 F. Supp. 278 (D.Colo. 1989).

Section 24.700 of 24 C.F.R. authorizes HUD office managers to impose an LDP on participants in HUD programs based on adequate evidence of, among other things, "[i]rregularities in a participant's or contractor's past performance in a HUD program." 24 C.F.R. § 24.705(a)(2). "Adequate evidence" is "[i]nformation sufficient to support the reasonable belief that a particular act or omission has occurred." 24 C.F.R. § 24.105.⁴

³The bid on the property at 2655 Knox Avenue North was rejected because too low. (GX. 24) The bid on the property at 2712-14 Penn Avenue North was accepted August 17, 1992, but later canceled. (TR. 15)

⁴"Adequate evidence" is to be contrasted with "preponderance of the evidence," which is defined in the regulations as "[p]roof by information that, compared with that opposing it, leads to the conclusion that the fact at issue is more probably true than not." 24 C.F.R. § 24.105(o).

Section 24.105(b) of 24 C.F.R. defines "affiliate" as follows:

Persons are affiliates of each other if, directly or indirectly, either one controls or has the power to control the other, *or*, a third person controls or has the power to control both. Indicia of control include, but are not limited to: interlocking management or ownership, identity of interests among family members, shared facilities and equipment, common use of employees, or a business entity organized following the suspension or debarment of a person which has the same or similar management, ownership, or principal employees as the suspended, debarred, ineligible, or voluntarily excluded person.

As an entity under the exclusive control of Respondent Wirth, REECM was an affiliate of Respondent Wirth from its formation until at least July of 1992. Evidence in the record indicates that after July of 1992 Mr. Brynestad became the sole owner of REECM at the cost of \$1.00. At this point, the corporation ostensibly became an affiliate of Mr. Brynestad. However, the formality of the corporate structure cannot be allowed to disguise reality. Piercing the corporate veil reveals that the corporation and the individual were, in fact, the same real party in interest. That is, in the context of the argument that Mr. Brynestad owned REECM, the individual and the corporation must be treated as the same entity. Therefore, a prohibition running against Mr. Brynestad likewise proscribed the activities of REECM.

Mr. Brynestad was not named in the LDP issued against Respondent Wirth on June 15, 1992, but he nevertheless fell within the scope of the LDP because it included all of Respondent Wirth's affiliates "as they are identified by standards in the regulations (24 CFR 24.105(b))." (Feeney LDP letter of June 15, 1992) In other words, the LDP included all of Respondent Wirth's affiliates, whether or not named and whether or not they were aware of or participated in the activities that caused the LDP.

An affiliate or organizational element may be included in a limited denial of participation solely on the basis of its affiliation, and regardless of its knowledge of or participation in the acts providing cause for the sanction.

(24 C.F.R. § 24.710(c)) In short, the LDP issued on June 15, 1992, against Respondent Wirth and his affiliates also prohibited Mr. Brynestad and REECM from participating in the Department's property sales disposition program. Yet on August 10, 1992, knowing that an LDP had been imposed against Respondent Wirth and his affiliates, Mr. Brynestad and his corporation submitted a bid to purchase a HUD-owned property. (TR. 92) That bid violated the terms of the LDP issued on June 15, 1992. The issue is whether Respondent Wirth is responsible for the violation.

Mr. Brynestad and Respondent Wirth are affiliates of each other because Mr. Brynestad is employed by and subject to the control of Respondent Wirth. Under the regulations, persons are affiliates of each other if one has the power to control the other. Respondent Wirth nevertheless argues that he was not responsible for and did not control the activities of Mr. Brynestad and REECM in connection with the attempted purchase of HUD-owned properties. The record contains more than adequate evidence to refute that argument.

According to Respondent Wirth, he and his wife "sold" REECM to Mr. Brynestad for \$1.00 only a few weeks after issuance of the LDP of June 15, 1992. The timing and economics of this transaction alone make it suspect. Furthermore, the "sale" of the corporation was not memorialized in a written contract. Although a stock certificate in the record shows the transfer of 1,000 shares of stock from Respondent Wirth and his wife to Mr. Brynestad on July 23, 1992, the transfer certificate was neither notarized nor witnessed, and Mr. Brynestad's later conversations with a HUD official suggest that the certificate was completed only after HUD raised questions about the Penn Avenue North transaction. (TR. 91, 95, 112)

Suspicion increases upon examination of the circumstances surrounding the bids for the HUD-owned properties. Mr. Brynestad signed the bids as "Vice-President." It is unlikely that someone who truly believed himself the newly installed sole owner and operator of a corporation would declare himself only a junior corporate officer in formal contract documents. According to State of Minnesota records, at the time the bids were submitted to HUD, Respondent Wirth was the chief executive officer of the corporation. (GX. 26) It is far more likely that the Minnesota records reflected reality than that Mr. Brynestad signed the bids as "Vice-President" because, as he incredibly claimed, he had not had time to get himself appointed president by a board of directors whose identity he could not or would not disclose.⁵ (TR. 92)

All of Mr. Brynestad's activities concerning the bids for HUD-owned properties occurred on company time using the services and facilities provided by Mr. Wirth and his affiliated companies, such as stationery, a telefax machine, copier, and telephones. (TR. 197; GX. 33-37)

Before bidding on HUD's properties, Mr. Brynestad had less than three years experience in the real estate business and no experience buying and selling property in his own behalf. Despite his lack of experience, he testified that unnamed family friends (whom he did not want to identify) agreed, without any security whatsoever, to finance

⁵According to Minnesota Department of State records, Respondent Wirth was still listed as chief executive officer of REECM as of April 2, 1993. (GX. 26)

his transactions--at a cost of about \$23,000 on the Penn Avenue North property alone.⁶ (TR. 193) This testimony was uncorroborated, self-serving, and incredible.

Respondent Wirth admitted that he participated in the transaction by searching for title insurance for the Penn Avenue North property.⁷ But he claims that he acted only in response to Mr. Brynestad's request for assistance, and that he agreed to teach Mr. Brynestad how to secure title insurance out of charitable motives alone. (TR. 202, 214, 243) This explanation will not wash. Mr. Brynestad neither witnessed nor participated in Respondent Wirth's telephone conversations seeking title insurance. (TR. 243-44) Without participating personally in the search for title insurance, Mr. Brynestad could not have learned anything from it that he could not have learned from talking to Respondent Wirth. In other words, Respondent Wirth need not have participated in the search for title insurance on the Penn Avenue North property in order to teach his employee all he knew about the subject.

In his conversations with representatives of two title companies, Respondent Wirth did not identify himself as an agent working on behalf of Mr. Brynestad; rather, he represented himself as an agent for the buyer, REECM, then headed by Respondent Wirth, according to State of Minnesota records. (TR. 70, 206; GX. 26) As a result of their contacts with Respondent Wirth and Mr. Brynestad, both title insurance company representatives concluded, independent of HUD influence, that Respondent Wirth was the real party in interest in the Penn Avenue North transaction, not Mr. Brynestad. (TR. 66-86; GX. 28-31)

In sum, the record contains adequate evidence to conclude that in August of 1992 Mr. Brynestad acted as a front-man for an attempted evasion of the LDP of June 15, 1992, by Respondent Wirth.

⁶Mr. Brynestad was not asked whether the unnamed family friends were Respondent Wirth and his wife.

⁷A "participant" includes "any person who acts on behalf of or is authorized to commit a participant in a covered transaction as an agent or representative of another participant." (24 C.F.R. § 24.105(m))

Even if we were to accept, *arguendo*, Respondent Wirth's incredible contention that he participated in the transaction only for the purpose of teaching Mr. Brynestad about title insurance, that contention itself condemns Respondent Wirth. The LDP of June 15, 1992, prohibited him from participating as a principal in a covered transaction in any capacity where he could exercise a "critical influence" on the transaction. (24 C.F.R. § 24.105(m) and (p)) By guiding and directing title insurance decisions, Respondent Wirth exercised critical influence on the Penn Avenue North transaction, a "covered" transaction within the meaning of the regulations. (24 C.F.R. § 24.110(a)(1)) Even if, as he claims, he did not stand to reap any direct financial gain from the transaction, he nevertheless eventually would benefit from the increased skills Mr. Brynestad presumably acquired as a result of Respondent Wirth's tutelage. When he used HUD's property disposition program as a teaching vehicle, he created a more knowledgeable employee who, by virtue of that increased knowledge, became more valuable to Respondent Wirth. In short, Respondent Wirth used HUD's property disposition program for his own benefit during a period when he was prohibited from participating in the program. That participation was seriously irresponsible, violated the outstanding LDP of June 15, 1992, and created an "irregularity" in a participant's past performance in a HUD program. (24 C.F.R. § 24.705(a)(2)) The manager of the Minneapolis-St. Paul Office of HUD therefore had cause to issue the LDP against Respondent Wirth and his affiliates on September 30, 1992. The record contains no evidence to mitigate the offense.

Respondents complain that the LDP of September 30, 1992, was issued improperly because it arises out of the LDP of June 15, 1992, which was itself improperly issued. That complaint has no merit. Whether or not the first LDP was valid is irrelevant for purposes of deciding the validity of the second. If a participant or contractor were permitted to violate an allegedly invalid LDP during the period between its issuance and the conclusion of the hearing on its merits, then HUD office managers and similarly authorized HUD officials would be unable to protect the Government from irresponsible participants and contractors while they contest LDPs issued against them.⁸ That process typically takes at least several months and sometimes more than a year. It clearly would be contrary to the public interest if a HUD office manager were unable to take immediate steps to reduce the risk of injury at the hands of persons whose conduct appears threatening.

It makes no difference that the scope of the LDP of June 15, 1992, was narrowed after HUD officials met with Respondent Wirth and his affiliates in October and November of 1992. The LDP of September 30, 1992, was based on conduct that occurred *before* modification of the LDP of June 15, 1992. It is at least seriously irresponsible if not dishonest for a participant or contractor to violate the terms of an LDP in the belief that it is invalid or in the expectation that its terms will be modified in the future to permit the violative conduct.

⁸ See 24 C.F.R. § 24.700 for a list of all HUD officials authorized to issue an LDP.

Conclusion

Upon careful consideration of the record, I conclude that the manager of the Minneapolis-St. Paul Office of HUD exercised sound discretion in the best interests of the Government when he issued the LDP against Respondent Wirth and his affiliates on September 30, 1992.

/s/

THOMAS C. HEINZ
Administrative Law Judge

Dated: November 12, 1993

